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No. 46

In the Supreme Court of the United States

October Term, 1935.

THE UNITED STATES OF AMERICA, *Petitioner,*

vs.

ROGER KESTERSON AND BERNORD ROBERTS.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Tenth Circuit.

BRIEF FOR THE RESPONDENTS.

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BRIEF *for the* RESPONDENTS.

Statement.

On October 5, 1934, the United States Grand Jury for the Northern District of Oklahoma returned an indictment charging that respondents on August 17, 1934, carried on the business of a retail liquor dealer in that district, contrary to the laws of the State of Oklahoma, without having paid the special excise tax of $1,000.00 provided by Section 701 of the Revenue Act of 1926 (U. S. C. A., Title 26, Section 206).

On November 9, 1934, respondents filed a demurrer to the indictment on the grounds *(a)* that Section 701 was un-

constitutional in that it violated the provisions of Article 1, Section 8, Clause 1, of the Constitution requiring that all duties, imposts and excises be uniform throughout the United States, and *(b)* that the "excise tax therein provided for is in the nature of penalty and not for the purpose of raising revenue, in connection with matters over which the Congress has no authority to legislate."

The District Court overruled the demurrer. Thereupon respondents entered *nolo contendere* pleas, were found guilty as charged, and sentence imposed, Kesterson being sentenced to serve six months in jail and to pay a fine of $500.00 and Roberts being sentenced to serve ninety days in jail and to pay a fine of $100.00.

The respondents appealed to the Circuit Court of Appeals for the Tenth Circuit, which reversed the judgments of conviction, holding that Section 701 "was prescribed as a regulatory measure to provide an additional penalty • • • to aid in the suppression of dealing in liquor, a subject over which Congress has had no power since the repeal of the Eighteenth Amendment," and that Section 701 imposes not an excise tax but a penalty dealing with a subject left or committed by the Constitution to the control of the states. *Kesterson* v. *United States,* 76 F. (2d) 913.

The decision of the Circuit Court sustains the second ground contained in respondents' demurrer. The court deemed it unnecessary to pass upon the first ground urged in the demurrer, that is, the question of uniformity, because of its holding that Section 701 was not a tax but a penalty.

ARGUMENT.

I.

Section 701 of the Revenue Act of 1926 is unconstitutional because it imposes a penalty and not a true excise tax, and fell with the repeal of the Eighteenth Amendment.

II.

If said section 701 be held to impose an excise tax and not a penalty it is unconstitutional because it violates article 1, section 8, clause I of the Constitution, in that it lacks uniformity as therein required.

We respectfully submit that the first question thus presented for determination, if decided in favor of respondents, is decisive of the entire controversy, this question being: Is the exaction levied by Section 701 a tax or a penalty? However, we deem it proper to argue both propositions upon which we rely. These will be presented separately.

I.

At the outset we believe it must be conceded that, if the exaction is a penalty, it fell with the repeal of the Eighteenth Amendment. *United States* v. *Chambers*, 291 U. S. 217.

Section 701 first existed, but in slightly different form, in Section 1001 of the Revenue Act of 1918, approved February 24, 1919. This was after the ratification of the Eighteenth Amendment, which was on January 29, 1919, although same did not become effective until one year thereafter. Acts of Congress, creating war-time prohibition, had, previous to the ratification of the Eighteen Amendment, been

passed and approved. The National Prohibition Act, dependent for its constitutionality on the amendment, was enacted October 28, 1919, but was not operative until the effective date of the amendment—January 29, 1920.

Thereafter, in its then form, Section 701 was re-enacted as subsection 12 of Section 1001 of the Revenue Act of 1921, and later as subsection 9 of Section 701 of the Revenue Act of 1924, and finally in its present form as Section 701 of the Revenue Act of 1926.

In addition to the tax against unlawful liquor dealers many lawful occupations were the subject of taxation in the Revenue Acts of 1918, 1921 and 1924. All except the unlawful liquor dealer are found omitted in the Revenue Act of 1926, at which time the Eighteenth Amendment and the National Prohibition Act were in force.

Let us then first inquire into the facts which we contend show that Congress, in 1926, was actuated primarily by an attempt to suppress the unlawful traffic in liquor by the exaction in question instead of an attempt to raise revenue. It should be remembered that the many occupations included in the several Revenue Acts exacted prior to 1926, although affording a source of great revenue, were omitted from the act in question. In the House Report on the Revenue Bill of 1918, in which Section 701 had its origin, it appeared that one of the principal objects of the bill was to aid in financing the war, and The Committee on Ways and Means estimated that the special taxes therein provided for would yield about $165,000,000.00 annually. In 1926, elimination of the occupational taxes was occasioned by an increased surplus in the Treasury which permitted a general reduction in taxes. Yet the one occupation retained by the

Act of 1926 was unlawful under existing law on account of which no revenue from that source could be expected. Furthermore, it is a matter of history that during the prohibition era, and especially in 1926, great efforts were exerted by the Government to suppress the unlawful traffic in liquor and sterner penalties for violation were constantly being urged. However, prior to 1929, these penalties were comparatively light. By the Act of March 2, 1929, they were greatly increased, fixing a maximum fine of $10,000.00 and maximum imprisonment of five years. On July 30, 1926, shortly after the effective date of the Revenue Act of 1926, the Treasury Department, by its regulation numbered 3911, specifically construed and held the exaction by the act to be a penalty and not a tax.

These facts, we believe, tend to demonstrate that the exaction of the $1,000.00 excise by the Act of 1926 is not a true tax but is a penalty involving the idea of punishment for infraction of the law.

Under the provisions of Section 205, Title 26, U. S. C. A., wholesale liquor dealers are required to pay an annual excise tax of $100.00, retail dealers $25.00, wholesale dealers in malt liquors $50.00, and retail dealers in malt liquors $20.00. Under Section 701, however, all liquor dealers, whether wholesale or retail, in "dry" states or communities, are required to pay the same sum, namely, $1,000.00, annually, and in the case of retail dealers a sum forty times greater than a similar occupation in so-called "wet" states. It is significant that Section 701 exacts the same amount from all kinds of handlers of intoxicating liquor instead of, as liquor-taxing acts do, and as is provided by Section 205, Title 26, U. S. C. A., making the exaction fit the business

done. It cannot be contended that there is no logic in this argument because all handlers of intoxicating liquors contrary to state laws or municipal ordinances "were in the same boat" because such was not the case. In fact, violations of state and municipal laws and ordinances placed the violators in different categories, because some thereby committed felonies while others misdemeanors punishable by small fines.

In determining the question before us we should endeavor to distinguish between a "tax" and a "penalty." In the case of the *United States* v. *La Franca,* 282 U. S. 568, this court, in passing upon Section 701 of the Revenue Act of 1924, said:

> "A tax is an enforced contribution to provide for the support of government; a penalty, as the word is here used, is an exaction imposed by statute as punishment for an unlawful act. The two words are not interchangeable one for the other. No mere exercise of the art of lexicography can alter the essential nature of an act or a thing; and if any exaction be clearly a penalty it cannot be converted into a tax by the simple expedient of calling it such. * * *"

In *Lipke* v. *Lederer,* 259 U. S. 557, we find:

> "The mere use of the word 'tax' in an act primarily designed to define and suppress crime is not enough to show that within the true intendment of the term a tax was laid. * * * When by its very nature the imposition is a penalty, it must be so regarded. *Helwig* v. *United States,* 188 U. S. 605. Evidence of crime (section 29) is essential to assessment under section 35. It lacks all the ordinary characteristics of a tax, whose primary function 'is to provide for the support of government' and clearly involves the idea of punishment for infraction of law—the definite function of a penalty. *O'Sullivan* v. *Felix,* 233 U. S. 318, 324."

We believe that the case of *United States* v. *La Franca, supra,* is decisive of the question under discussion. It is true that the court there had under consideration Section 701 of the Revenue Act of 1924. But little difference is noted between that act, as pertaining to unlawful liquor dealers, and the same section in the Revenue Act of 1926. By the terms of Section 52, Title 27, U. S. C. A., being c. 85, Title 11, Section 35, Act of October 28, 1919, the exaction was doubled. The Government in the *La Franca* case sought judgment for the doubled tax, after conviction of La Franca for infraction of the law that subjected him thereby to payment of the tax. He entered a defense of double jeopardy, contending that the tax levied under Section 701 of the Act of 1926, doubled by the section of the National Prohibition Act above mentioned, was a penalty for infraction of the law and not a true excise tax. This court sustained that contention, saying:

> "Of the four items involved, two unmistakably are penalties, and are so denominated. The other two, notwithstanding they are called taxes, are in their nature also penalties."

It is argued by counsel for petitioner herein, and in the companion case of *United States* v. *Constantine,* No. 40, October Term, 1935, that Section 701 became a penalty, and was so held, because of the provisions of the previously enacted section of the National Prohibition Act referred to. If this argument is sound, then why was not judgment entered in favor of the United States for the tax levied by the revenue act in the amount therein imposed, and not for the double amount sought? In other words, if the tax fixed by Section 701 of the Revenue Act of 1924 was a true excise tax and not a penalty, why was the Government denied

judgment for the amount thereof? The answer is found in the decision—that same is a penalty. It is to be remembered that this court has held that a tax on intoxicating liquor does not cease to be such because the sovereign has declared none shall be manufactured. *United States* v. *One Ford Coupe*, 272 U. S. 321.

Counsel for petitioner, in their brief in the *Constantine* case, take the view that the excise tax in question was a true tax when first imposed by the Revenue Act of 1918, became a penalty during the period the National Prohibition Act was in force, and thereafter reverted to its true status as a tax (p. 22). A complete answer to this strange contention is that the section in controversy between us was enacted into law in 1926, during the era of national prohibition. So that, at the time of its very enactment it became a penalty, yet, they argue that same is a true excise tax imposed for the support of government.

We respectfully submit that the decision of the Circuit Court of Appeals is correct and should be affirmed.

II.

If the exaction provided by Section 701 is not a penalty but a true tax, we submit it is unconstitutional because of non-uniformity. Article 1, Section 8, Clause 1, of the Constitution requires that "all duties, imposts and excises shall be uniform throughout the United States."

By the provisions of Section 205, Title 26, U. S. C. A., retail liquor dealers are taxed $25.00 and by Section 206 (Section 701, Revenue Act of 1926) $1,000.00 in "dry" states or municipalities. The subject of the two so-called taxes is the same, namely, retail liquor dealers. The "rate" or

"amount" of the exaction varies according to state laws or local municipal regulations or ordinances. It is our contention that the "rate" or "amount" of an excise must be the same throughout the United States and must operate uniformly from a geographical standpoint; in other words, that Congress is prohibited from levying excises upon one subject of taxation in different amounts or at different rates in the different states of the Union.

This court has held that the uniformity required by the Constitution has reference to the various localities in which the tax is intended to operate and has always been used with reference purely to geographical uniformity and as synonymous with the expression, "to operate generally throughout the United States." *Head Money Cases,* 112 U. S. 580; *Billings* v. *United States,* 232 U. S. 261; *Knowlton* v. *Moore,* 178 U. S. 41.

We concede that differences of state law which may bring a person within or without the category designated by Congress as taxable, may not be read into a revenue act to spell out a lack of uniformity *(Poe* v. *Seaborn,* 282 U. S. 101), but we contend that the act itself may not create the lack of uniformity and comply [illegible] the constitutional provision.

In *United States* v. *Singer,* 15 Wall. 111, an attack for alleged non-uniformity was made upon the Act of July 20, 1868, imposing excises on distilled spirits, the distiller being assessed 80% of the producing capacity of his distillery, and if the spirits actually produced by him exceeded this 80% he was required to pay an excise upon the excess. The distiller in the *Singer* case had actually produced less than 80% of his capacity and objected to the assessment of 80%

for that reason. On the question of uniformity, this court said:

> "The law is not, in our judgment, subject to any constitutional objection. The tax imposed upon the distiller is in the nature of an excise, and the only limitation upon the power of Congress in the imposition of taxes of this character is that they shall be 'uniform throughout the United States.' The tax here is uniform in its operation; that is, it is assessed equally upon all manufacturers of spirits wherever they are. The law does not establish one rule for one distiller and a different rule for another, but the same rule for all alike."

Section 701 fixes one tax for one liquor dealer while Section 205 fixes a different tax for another liquor dealer.

In *Florida* v. *Mellon*, 273 U. S. 12, an attack was made on the inheritance tax act of 1926 for non-uniformity because the State of Florida did not impose inheritance taxes while other states did, the Act of Congress providing for credit on federal tax of sums paid on state inheritance taxes. The court said:

> "The contention that the federal tax is not uniform because other states impose inheritance taxes while Florida does not, is without merit. Congress cannot accommodate its legislation to the conflicting or dissimilar laws of the several states nor control the diverse conditions to be found in the various states which necessarily work unlike results from the enforcement of the same tax. All that the Constitution (Art. 1, Sec. 8, cl. 1) requires is that the law shall be uniform in the sense that by its provisions the rule of liability shall be alike in all parts of the United States."

Section 701 cannot be sustained on the ground that it operates uniformity in all states where the subject of the

tax—the business of a retail liquor dealer—is prohibited by state law. The non-uniformity, which the law itself by its very terms sets up, exists even in those states where by statute the subject of the tax is not prohibited. We find that a municipal ordinance, prohibiting the business of a liquor dealer under local option, creates a liability to pay $1,000.00 per annum instead of $25.00 per annum, notwithstanding the state in which the municipality is located does not by statute prohibit same.

Counsel for petitioner rely upon *Clark Distilling Co.* v. *Western Maryland Ry. Co.*, 242 U. S. 311, but we find therein the following:

> "So far as uniformity is concerned, there is no question that the act uniformly applies to the conditions which call its provisions into play—that its provisions apply to all states—so that the question really is a complaint as to the want of uniform existence of things to which the act applies and not to an absence of uniformity in the act itself. * * *"

As heretofore stated, we submit that the act itself, by its wording, sets up the absence of uniformity, which is prohibited by the Constitution.

Conclusion.

For the reasons stated, we respectfully submit that Section 701 of the Revenue Act of 1926 fell with the repeal of the Eighteenth Amendment because it imposes a penalty and not an excise tax; and that, in any event, the same violates the provision of the Constitution referred to because of the absence of uniformity in its terms.

The judgment of the Circuit Court of Appeals shou
therefore be affirmed.

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